

Function 570: Medicare

Function 570 (Medicare) includes only the Medicare program. Appropriated funds are used to administer and monitor the Medicare program. Medicare benefits comprise almost all of the mandatory spending in this function.

Medicare Administration

Medicare's administrative budget is \$5.0 billion in 2007, of which \$3.1 billion is appropriated to the Centers for Medicare and Medicaid Services (CMS), and the remainder is transferred from the Medicare Trust Funds to other agencies for Medicare-related administrative activities. The overall budget is a \$56 million increase above the 2006 level, while the CMS appropriation is \$5 million below the 2006 enacted level. The budget includes \$35 million in new user fees, and will reduce the direct appropriation by a comparable amount if the user fees are enacted. The new user fees are to charge health-care facilities for follow-up surveys that occur when the facility has been cited for deficiencies during certification/recertification or complaint surveys.

Medicare Benefits and Spending Trends

Medicare Spending in 2007 — The budget projects Medicare net mandatory spending of \$389.2 billion in 2007 under current law.³

Medicare Prescription Drug Spending — The Administration's new estimates for the prescription drug benefit show that spending projections for the Medicare drug benefit have dropped. Previously, the Administration estimated net Medicare spending on the drug benefit from 2006 to 2015 at \$926 billion. Including interactions with Medicaid, the Administration estimated net federal spending at \$737 billion.

The Administration's new estimates project net *Medicare* spending of \$797 billion over that time period, a drop of \$130 billion. The Administration's estimates for net *federal* spending, including Medicaid interactions, have dropped to \$678 billion, a decline of \$59 billion.

For the 2007 to 2016 budget window, the Administration projects \$1.1 trillion in total spending on the drug benefit. Including beneficiary premiums and receipts from states (the "clawback"), net Medicare spending is projected at \$900 billion. The calculation for net federal spending is not available.

³Net mandatory spending reflects total spending on benefits, less the amount collected from beneficiaries in the form of premiums. This number excludes administrative costs.

Medicare Prescription Drug Benefit (Dollars in Billions)			
	2006 - 2015 (7/05 estimate)	2006- 2015 (1/07 estimate)	2007 - 2016 (1/07 estimate)
Gross Medicare Spending for Drug Benefit	1207	1015	1144
Beneficiary Premiums	-147	-120	-138
Medicaid "Clawback"	-134	-98	-107
Net Medicare Spending for Drug Benefit	926	797	900
Federal Medicaid Savings	-189	-119	NA
Net Federal Cost (Medicare and Medicaid)	737	678	NA

The Administration claims that the drop in spending projections is proof that the drug benefit is lowering drug costs for seniors. However, others criticize that logic, pointing to evidence that Part D drug prices are still higher than those paid by the Department of Veterans' Affairs, or available at Drugstore.com, Costco, or in Canada. Furthermore, many analysts believe that the bids submitted by many Part D drug plans (which drive the premiums and government payments) were set purposefully low. The strategy for many plans is to "take a loss leader position," grab market share, and drive out competition so that they can secure a position in the market and perhaps drive up premiums in the future.

Medicare Legislative, Regulatory and Administrative Policies

Legislative Cuts to Medicare of \$105 Billion Over Ten Years — The budget makes legislative cuts to Medicare of \$35.9 billion over five years and \$105 billion over ten years by reducing payments for providers in traditional Medicare. The budget also includes regulatory cuts of \$7.9 billion over five years and \$19.0 billion over ten years. Excluding already published regulations, the regulatory savings are \$5.4 billion over five years and \$13.2 billion over ten years.

- ***Cuts Inpatient Hospital Update*** — The budget cuts payments for inpatient hospitals by providing an update for 2007 of market basket minus 0.45 percentage points, and updates for 2008 and 2009 of market basket minus 0.4 percentage points. This policy saves \$6.6 billion over five years, and \$17.4 billion over ten years.

Medicare Legislative Cuts of \$105 Billion Over Five Years
(dollars in billions)

	<u>2007 - 2011</u>	<u>2007 - 2016</u>
Cut Inpatient Hospital Update	-6.6	-17.4
Cut Skilled Nursing Facility Update	-5.1	-12.4
Cut Home Health Update	-3.5	-9.0
Cut Inpatient Rehabilitation Facility Update	-1.6	-3.9
Cut Hospice Update	-0.6	-1.5
Adjust Payment for Hip and Knee Replacements in Post-Acute Care Settings	-2.4	-5.8
Cut Outpatient Hospital Update	-1.5	-4.6
Cut Ambulance Update	-0.3	-0.9
Expand Competitive Bidding to Laboratory Services	-1.4	-5.2
Pay for Short-Term Power Wheelchairs Based on Actual Use	-0.5	-1.1
Limit Oxygen Rental Period to 13 Months	-6.6	-18.0
Eliminate Payments for Bad Debt	-6.2	-22.5
Expand Application of Medicare Secondary	-1.6	-3.8
Eliminate Indexation of Income-Related Premium Thresholds*	-1.9	-10.1
Premium Interactions	3.8	11.2
Total Medicare Legislative Cuts	-35.9	-105.0

* This proposal includes savings from (1) beneficiaries not signing up for Medicare (-\$40 million over five years, and -\$350 million over ten years) and (2) increased premium collections (-\$1.9 billion over five years, and -\$9.8 billion over ten years), for total savings reflected in the table.

- ***Cuts Skilled Nursing Facility Update*** — The budget cuts payments for skilled nursing facilities by freezing payment rates for 2007 at the 2006 level and providing an update for 2008 and 2009 of market basket minus 0.4 percentage points. This policy saves \$5.1 billion over five years, and \$12.4 billion over ten years.
- ***Cuts Home Health Update*** — The budget cuts payments for home health providers by freezing payment rates at the 2006 level for calendar year 2007, and providing an update for calendar years 2008 and 2009 of market basket minus 0.4 percentage points. This policy saves \$3.5 billion over five years and \$9.0 billion over ten years.

- ***Cuts Inpatient Rehabilitation Facility Update*** — The budget cuts payment for inpatient rehabilitation facilities (IRF) by freezing payments rates for 2007 at the 2006 level and providing an update for 2008 and 2009 of market basket minus 0.4 percentage points. The policy saves \$1.6 billion over five years, and \$3.9 billion over ten years. The budget also includes further cuts to IRFs via regulatory changes, as discussed below.
- ***Cuts Hospice Update*** — The budget cuts payments to hospice providers by providing an update of market basket minus 0.4 percentage points for 2007 through 2009. This policy saves \$0.6 billion over five years, and \$1.5 billion over ten years.
- ***Adjusts Payments for Hip and Knee Replacements*** — The budget adjusts payments for hip and knee replacements so that the payment rates across different post-acute settings are better aligned. This policy saves \$2.4 billion over five years and \$5.8 billion over ten years. The budget also includes further cuts to long-term care hospitals via regulatory changes, as discussed below.
- ***Expands Competitive Bidding to Laboratory Services*** — The budget extends competitive bidding to laboratory services, similar to the competitive bidding system currently in place for durable medical equipment. This policy saves \$1.4 billion over five years and \$5.2 billion over ten years.
- ***Pays for Short-Term Power Wheelchairs Based on Actual Use*** — The budget changes payments for short-term power wheelchair usage so that payments are based on actual usage time. This policy saves \$0.5 billion over five years and \$1.1 billion over ten years. The budget also includes further cuts to wheelchair payments via regulatory changes, as discussed below.
- ***Limits Oxygen Rental Period to 13 Months*** — The budget changes payments for oxygen equipment so that the beneficiary owns the equipment after 13 monthly rental payments. This policy was omitted from the Republican spending cut reconciliation bill at the last minute. This policy saves \$6.6 billion over five years and \$18.0 billion over ten years.
- ***Eliminates Payments for Bad Debt*** — Currently, Medicare reimburses some Medicare providers for 70 to 100 percent of their bad debt (from uncollected cost-sharing owed by Medicare patients). The budget eliminates Medicare reimbursements for bad debt, for savings of \$6.2 billion over five years and \$22.5 billion over ten years. This policy affects inpatient hospital payments, skilled nursing facilities, critical access hospitals, rural health clinics, community mental health centers, and federally qualified health centers (FQHCs).

- ***Expands Application of Medicare Secondary Payer*** — Generally, Medicare is the “primary payer;” in most instances, it pays health claims first, with the beneficiary’s private or other public insurance filling in some or all of Medicare’s gaps. However, under the Medicare Secondary Program (MSP), there are certain situations where a beneficiary’s group health insurance, liability, workers’ compensation, or no-fault coverage pays health claims first, while Medicare is the secondary payer. The budget extends MSP status for End-Stage Renal Disease (ESRD) payments from 30 to 60 months and establishes a federal data-sharing clearinghouse for MSP, for savings of \$1.6 billion over five years and \$3.8 billion over ten years.
- ***Raises Medicare Premiums for Certain Beneficiaries*** — Under the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA), certain upper-middle income seniors will pay higher premiums for Medicare Part B starting in 2007. The income thresholds that trigger the higher premiums are supposed to be adjusted for inflation, but the budget removes this protection. If the premium is not indexed for inflation, more and more seniors will reach the income threshold for higher premiums every year. The Administration projects that 3.8 million seniors will pay higher premiums in 2016 under this policy, compared with 1.9 million seniors under current law in that same year. A total of \$10.1 billion of the \$105 billion in ten-year Medicare savings comes from this change. Of this amount, \$9.8 billion is from higher premium collections, and \$350 million is from benefit savings because some beneficiaries will no longer join Medicare.

Creates Automatic Across-the-Board Cut in Medicare — The MMA requires the Medicare trustees to estimate in each of their annual reports the point at which Medicare general revenues – as compared with premiums and payroll taxes – will finance at least 45 percent of Medicare costs. Once the trustees estimate in two successive reports that this 45-percent level will be reached within the next six years, the President is required to include a proposal in his next budget to cut Medicare spending. The budget builds on this provision, imposing an across-the-board cut to all Medicare providers of 0.4 percent in the year the threshold is exceeded if Congress does not enact spending cuts before then. The across-the-board cut will become deeper in each subsequent year, until legislation is enacted to cut spending.

Fails to Address Medicare Physician Payment Cut — The recently passed Republican reconciliation spending cut bill prevented a scheduled 4.4 percent cut in physician payments for 2006, but physicians are still slated to receive a cut in 2007 and additional cuts in the following years. The budget does not include a fix for this Medicare physician payment issue – the budget just professes support for remedies that base physician payment updates on quality measures and that are budget neutral.

Fails to Address Overpayments to Medicare Advantage Plans — While the budget includes \$105 billion in Medicare cuts over ten years, none of those cuts address current overpayments to Health

Maintenance Organizations (HMOs) and Preferred Provider Organizations (PPOs) participating in the Medicare Advantage program. The Medicare Payment Advisory Commission recommends roughly \$50 billion in savings from Medicare Advantage plans (2006 to 2015) – the budget does not include any of those savings.

Medicare Health Savings Accounts — In the budget, the Administration announced it is developing new Medicare Health Savings Accounts options for beneficiaries. Additional details are not available.

Regulatory Cuts of \$19.0 Billion Over Ten Years — In addition to the legislative cuts, the budget also includes \$19.0 billion in regulatory cuts over ten years. Some of these regulatory changes were included in spending projections released by the Administration last year and have already been published as proposed regulations. Excluding already published regulations, the regulatory savings are \$5.4 billion over five years and \$13.2 billion over ten years.

- ***Cuts to Inpatient Rehabilitation Facilities*** — The budget includes regulatory cuts for inpatient rehabilitation facilities of \$2.0 billion over five years, and \$4.7 billion over ten years. These regulatory changes include a 1.9 percent reduction in payments in 2006, and a 2.3 percent reduction in payments for 2007. Excluding the already published regulation for 2006, the savings are \$1.1 billion over five years and \$2.6 billion over ten years.
- ***Cuts to Long-Term Care Hospitals*** — The budget includes regulatory cuts for long-term care hospitals (LTCH) of \$2.5 billion over five years and \$6.1 billion over ten years. These regulatory changes include a freeze in payment rates at the 2006 level for 2007 and 2008 and a modification to payments for short-stays in LTCHs.
- ***Cuts for Durable Medical Equipment*** — The budget makes regulatory changes to payments for wheelchairs and other forms of durable medical equipment, for savings of \$1.8 billion over five years and \$4.6 billion over ten years.
- ***Cuts for Medicare Part B Covered Drugs*** — Certain prescription drugs, such as those administered by a physician, are paid for under Medicare Part B, rather than under the new prescription drug benefit. The budget includes changes to the dispensing fee for inhalation drugs, and the supplying fee for oral drugs, for savings of \$1.6 billion over five years and \$3.6 billion over ten years. These changes were included in the physician fee schedule for 2006.